



**DEPARTMENT OF BUSINESS,
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Statement of
RICHARD C. LIM
Director
Department of Business, Economic Development, and Tourism
before the
COMMITTEE ON FINANCE
Tuesday, February 27, 2012
1:00 PM
State Capitol, Conference Room 308
In consideration of
HB 1511 HD1 RELATING TO HIGH TECHNOLOGY

Chair Oshiro, Vice Chair Lee, and Members of the Committee on Finance: Thank you for this opportunity to submit testimony on HB 1511 HD1.

The Department of Business, Economic Development and Tourism (DBEDT) supports the intent of HB 1511 HD1. DBEDT supports the effort to reinstate the R&D tax credit as a mechanism to promote high technology and innovation as an emerging industry within the State. DBEDT also supports extending the MIC land lease. The High Technology Development Corporation (HTDC) plays a key role in economic development for the high technology industry within the State. HTDC is also assisting DBEDT by serving a leading role in the Governor's Hawaii Broadband Initiative. Their stability for the next 6 years is critical for HBI. DBEDT will continue to assist HTDC in finding both a near-term and long-term resolution for their land lease.

Thank you for the opportunity to submit testimony.



UNIVERSITY OF HAWAII SYSTEM

Legislative Testimony

Testimony Presented Before the
House Committee on Finance
February 27, 2012 at 1:00pm
by

James R. Gaines
Vice President for Research, University of Hawai'i

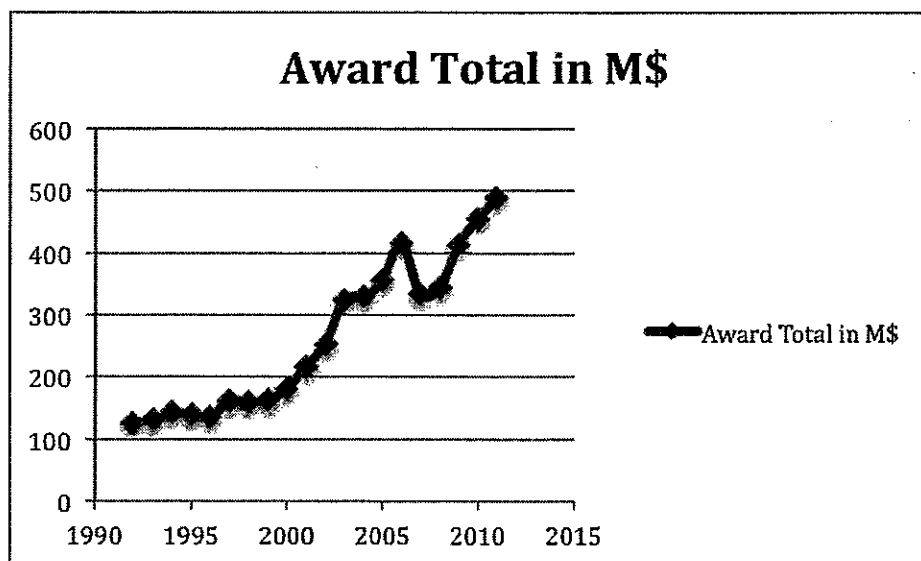
HB 1511 HD1 - RELATED TO HIGH TECHNOLOGY

Chair Oshiro, Vice Chair Lee and members of the committee:

The University strongly OPPOSES the section of this bill that requires the University to extend the lease of the Mānoa Innovation Center to HTDC for 25 more years after the present lease expires in 2015. The University has no position on Section 2.

In 1990 the University of Hawai'i (UH) entered into an agreement under which the (then) new Mānoa Innovation Center (MIC), constructed on University land, was to be leased to the High Technology Development Corporation (HTDC) for a 25-year term, after which the facility was to revert to UH. All parties agreed, in writing, to this arrangement.

Since the beginning of the current lease, University research awards have doubled in **each** of the past decades as shown by the graph below.



It is the goal of the University, in research, *to double the annual awards once more in the coming decade*. In order to accomplish this, new and remodeled facilities are essential and an expanded MIC will play an important role in achieving that goal.

It is important to emphasize the commitment of UH to the development of a robust research and technology industry in Hawai'i. Last year UH President Greenwood convened a blue ribbon task force to recommend key changes in how the University develops this research industry. Participants at our recently completed *E Kamakani Noi'i* conference further focused our ideas on what it will take to build a 21st century economy in Hawai'i.

We are still in the formative stages of defining exactly what form and structure will best support this needed innovation agenda. However, we expect that these activities will be based at the Mānoa Innovation Center, which is already a significant site for the University's research enterprise. In fact, UH and our related programs are already the single largest set of tenants in the facility and we are paying the largest portion of the rent, which goes to support HTDC operations. We could occupy all the existing space at MIC, with UH programs that are renting facilities elsewhere, immediately.

President Greenwood and UH leadership held preliminary discussions with the HTDC Executive Director and some of the HTDC board members. UH emphasized our willingness to let HTDC remain in the MIC facility after 2015 if they so choose. Our discussions further explored a range of possibilities, including HTDC playing a role in implementing the University's innovation agenda. These discussions are continuing and we will be happy to keep the Legislature informed of our progress.

The University does support the development of a technology park on O'ahu, the only island without such a capability. However, the Mānoa Innovation Center is not large enough to house the activities normally found within a technology park, so another venue should be found to provide full support for emerging technology businesses. HTDC would be the natural organization to lead such an initiative and UH would support them.

We believe this is an opportune time for the State to invest in the development of high technology to diversify and strengthen our economy. But this should not be done at the expense of research growth and the new innovation agenda being developed by UH.

We urge you to reject the section of this bill pertaining to the Mānoa Innovation Center and, at the very least, preserve the agreement made with UH at the time MIC was constructed.



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Written Statement of

KARL FOOKS

President

Hawaii Strategic Development Corporation

before the

HOUSE COMMITTEE ON FINANCE

February 27, 2012

1:00 PM

State Capitol, Conference Room 308

In consideration of

HB 1511 HD1 RELATING TO HIGH TECHNOLOGY.

Chair Oshiro, Vice Chair Lee, and Members of the Committee on Finance:

The Hawaii Strategic Development Corporation (HSDC) respectfully submits comments on HB 1511 HD1. The state tax credit for research activities sunset at the end of calendar year 2010. This tax credit program was an effective measure to support research and development activities, which in turn, foster and encourage the innovation essential to create high-wage job opportunities in our economy.

It is anticipated that use of this credit may fall below the levels of the previous tax credit as Federal spending on research activities has been reduced due to the elimination of earmarks. As the credit can only be claimed for actual expenditures made in Hawaii and only for 20% of the qualified expenditures, the cost of the program is partially offset by taxes paid on expenditures and payroll.

HSDC supports efforts to reinstate this tax credit, but has concerns about the definition of Qualified High Technology Business (QHTB) currently in HB1511 HD1. HSDC suggest a requirement that a QHTB be 1) a business, employing or owning capital or property, or maintaining an office, in this state; and 2) more than fifty per cent of its total business activities are qualified research.

Thank you for the opportunity to submit testimony on this bill.

Written Statement of
YUKA NAGASHIMA
Executive Director & CEO
High Technology Development Corporation
before the
COMMITTEE ON FINANCE
Tuesday, February 27, 2012
1:00 PM
State Capitol, Conference Room 308
In consideration of
HB 1511 HD1 RELATED TO HIGH TECHNOLOGY

Chair Oshiro, Vice Chair Lee, and Members of the Committee on Finance: Thank you for this opportunity to submit testimony on HB 1511 HD1.

The High Technology Development Corporation (HTDC) supports HB 1511 HD1 which extends R&D tax credits and requires the University of Hawaii (UH) to extend the current land lease for the Manoa Innovation Center (MIC) to the HTDC.

HTDC supports the effort to reinstate the R&D tax credit. With the elimination of federal earmark dollars, the tax credits granted by this bill are critically needed to support research and development activities in the state. Furthermore, the elimination of federal earmarks also suggests that the program may cost less than the \$11 million a year average referenced. HTDC respectfully suggests that tracking and reporting metrics similar to those agreed to by industry under last session SB753 HD2 Section 2 be considered for inclusion in this bill.

HTDC supports the extension of the current MIC land lease. Consistent with the University of Hawaii Innovation Council Recommendation, HTDC was formed by the State Legislature in 1983 to forward innovation and technology as a critical economic component of Hawaii. The HTDC manages the incubation facility at the MIC which was built by the State on land purchased by the UH under an agreement which expires in April 2015. The MIC incubation model provides a sustainable fund for a majority of the HTDC operation. If it is lost, the program cannot survive without an alternate revenue stream or additional state G-funds. Therefore, with the contract set to expire, HTDC must expend major efforts today to develop viable alternatives to ensure its future. UH has made clear that they intend to reclaim and repurpose the building in 2015 to build on their own research and innovation agenda.

The MIC facility is a highly desirable location for its proximity to UH faculty and students. Its separation from downtown also offers some strategic advantages for startups looking to keep a lower profile while they raise capital and develop their products. The facility is configured with a dense range of small offices which makes it cost efficient for a business startup. The small offices and flexible lease we offer allows a business to grow and shrink to meet its needs. HTDC has leveraged some of the larger offices into coworking spaces to allow more businesses to take advantage of our services, workshops, and programs.

While extending the land lease by 25 years would be the least disruptive to HTDC and the most economical resolution for the State, HTDC will continue to work with UH and legislators to find both a near-term and long-term solution. HTDC is supportive of UH's innovation agenda, technology commercialization, and workforce development initiatives.

Thank you for the opportunity to submit testimony on this bill.

TAXBILLSERVICE

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SUBJECT: INCOME, Extend tax credit for research activities

BILL NUMBER: HB 1511, HD-1

INTRODUCED BY: House Committee on Economic Revitalization and Business

BRIEF SUMMARY: Amends HRS section 235-110.91 to define "qualified high technology business" as a business, employing or owning capital or property, or maintaining an office, in this state; provided that: (1) more than 50% of its total business activities are qualified research and the business conducts more than 75% of its qualified research in this state; or (2) more than 75% of its gross income and funds are derived from qualified research; and this income is received from: (a) products sold from, manufactured in, or produced in this state; or (b) services performed in this state.

Extends the expiration of the tax credit for research activities from 12/31/10 to 12/31/15.

The University of Hawaii shall extend the current land lease agreement with the high technology development corporation on the same terms and for a period of at least 25 years from the expiration date of the existing lease.

This act shall be repealed on December 31, 2016 and provides that HRS section 235-110.91 shall be reenacted in the form in which it read on the day before the effective date of this act.

EFFECTIVE DATE: Tax years beginning after December 31, 2011

STAFF COMMENTS: The legislature by Act 178, SLH 1999, and Act 221, SLH 2001, enacted various tax incentives to encourage the development of high technology businesses in the state. These acts provided investment and research credits, as well as income exclusions, to attract high tech businesses to the state. This measure clarifies the definition of a qualified high technology business and extends the expiration of the tax credit from December 31, 2010 to December 31, 2015, which will perpetuate the financial drain on the state's revenues. It should also be remembered that the research credit is a refundable tax credit. Thus, should the amount of the credit exceed the taxpayer's income tax liability, any excess credit is a cash payment out of the state treasury to the claimant.

While the focus on high technology in the last few years is commendable, it fails to recognize that investments are made with the prospect that the venture will yield a profit. If the prospects for making a profit are absent, no amount of tax credits will attract investment from outside Hawaii's capital short environment. People do not invest to lose money. It should be remembered that until Hawaii's high cost of living can be addressed, all the tax incentives in the world will not make a difference in attracting new investments to Hawaii. The only attractive aspect for resident investors to plough money into such activities is the fact that the credit provides a way to avoid paying state taxes.

A former Hawaii resident who has been a success in the field of high technology pointed out recently what will make Hawaii conducive to high tech businesses and they are: (1) entrepreneurs, not capital, that comes first; (2) entrepreneurs coming from engineering schools and technology companies; (3) building a world class engineering school in Hawaii; (4) supporting internships at technology companies; (5) allowing our best children to go away to get a worldwide perspective; (6) not broadband passing through Hawaii that is a selling point; (7) that people fly direct and therefore is Hawaii's location in the middle of the Pacific an advantage?; (8) learning the rules of the game; (9) looking at Israel and learning from them; and (10) doing your own thing, being a copy cat does not work. At the heart of his remarks was the fact that in order to produce a high technology industry in Hawaii, those companies need to have access to institutions of higher education that are producing the people needed by the high technology industry. Without the academic synergy, Hawaii will never become a center for high technology activity. Thus, all of the tax incentives, like this measure embodies, will fall short of luring high technology firms to Hawaii.

One has to ask if the extension of the high technology tax credit is to mitigate the cost of doing business in Hawaii or subsidize conducting research in Hawaii as opposed to other parts of the country. Between the high cost of government regulation, the heavy burden of taxes, the draconian labor edicts, why would anyone want to undertake research in Hawaii? Given the fact that research runs the risk of any substantial rewards perhaps for years, the focus should be on improving the overall business environment in Hawaii as opposed to singling out on research in high technology. For years, Hawaii was known around the world for its research in agriculture undertaken by the Hawaii Sugar Planters' Association. Until the fading fortunes of the sugar industry, the state did little to support that research and then in its final days provided a million dollars per year on a matching basis. So instead of pursuing the elusive high technology industry research that is being conducted all over the nation, perhaps lawmakers should recognize the special niches that make Hawaii the perfect place to do that research and development. Thus, this extension continues the myopic view lawmakers seem to have about economic development and the future well-being of Hawaii.

Obviously the authors of this proposal would like to ignore the evaluation of these tax incentives done by UHERO a few years ago which basically condemned the credits as a waste of state resources as there is little evidence that the current program of tax credits has created substantial new employment or on-going enterprises. It is truly amazing that given the dire condition of the state's financial condition that lawmakers would continue to support unbridled drains of resources while at the same time proposing that the tax burden be increased on all other taxpayers. With declining revenues, every program from education to corrections to health services will be severely curtailed. If the state doesn't have the money to put textbooks in the schools why then do we need the highly touted, high-paying jobs the advocates for the industry promise? The next generation may not even know how to read given the cuts to the education budget.

Again, lawmakers must ask themselves whether or not this incentive is appropriate in these dire financial times or can more be done if government would just get out of the way and allow entrepreneurship to flourish unfettered. Given that there are many other proposals in the legislature to hike taxes or fees or adopt new fees to supplement and support new or existing programs, continuance of the research credit flies in the face of these tax increase proposals. Again, as noted above, when and until Hawaii has a topnotch academic community producing those who can contribute to the tome of

research available, such a credit will be a waste of taxpayer money. The resources needed to fund this credit would be better spent improving and enhancing the state's academic and intellectual community.

Finally, it should be noted that this state credit basically tracks the federal tax credit for research activities, including the disqualification for the credit should any part of the cost of the research be supported by federal grants. It would be interesting to learn how many of the claims for this state research credit were disqualified because all or a part of the research activities were paid for with funds from federal grants.

Digested 2/26/12